International Business Environments and Operations, 13/e

Part 6

Managing International Operations



Chapter 18

International Accounting Issues

Chapter Objectives

- To examine the major factors influencing the development of accounting practices in different countries
- To examine the global convergence of accounting standards
- To explain how companies account for foreign-currency transactions and translate foreign-currency financial statements
- To discuss different forms of performance evaluation of foreign operations and how foreign exchange can complicate the budget process
- To explain how arbitrary transfer pricing can complicate performance evaluation and control
- To introduce the balanced scorecard as an approach to evaluating performance

Crossroads of Accounting and Finance

- The accountant is essential in providing information to financial decision makers.
- MNEs must learn to cope with differing:
  - inflation rates
  - exchange-rate changes
  - currency controls
  - expropriation risks
  - customs duties
  - tax rates and methods of determining taxable income
  - levels of sophistication of local accounting personnel
  - local and home-country reporting requirements

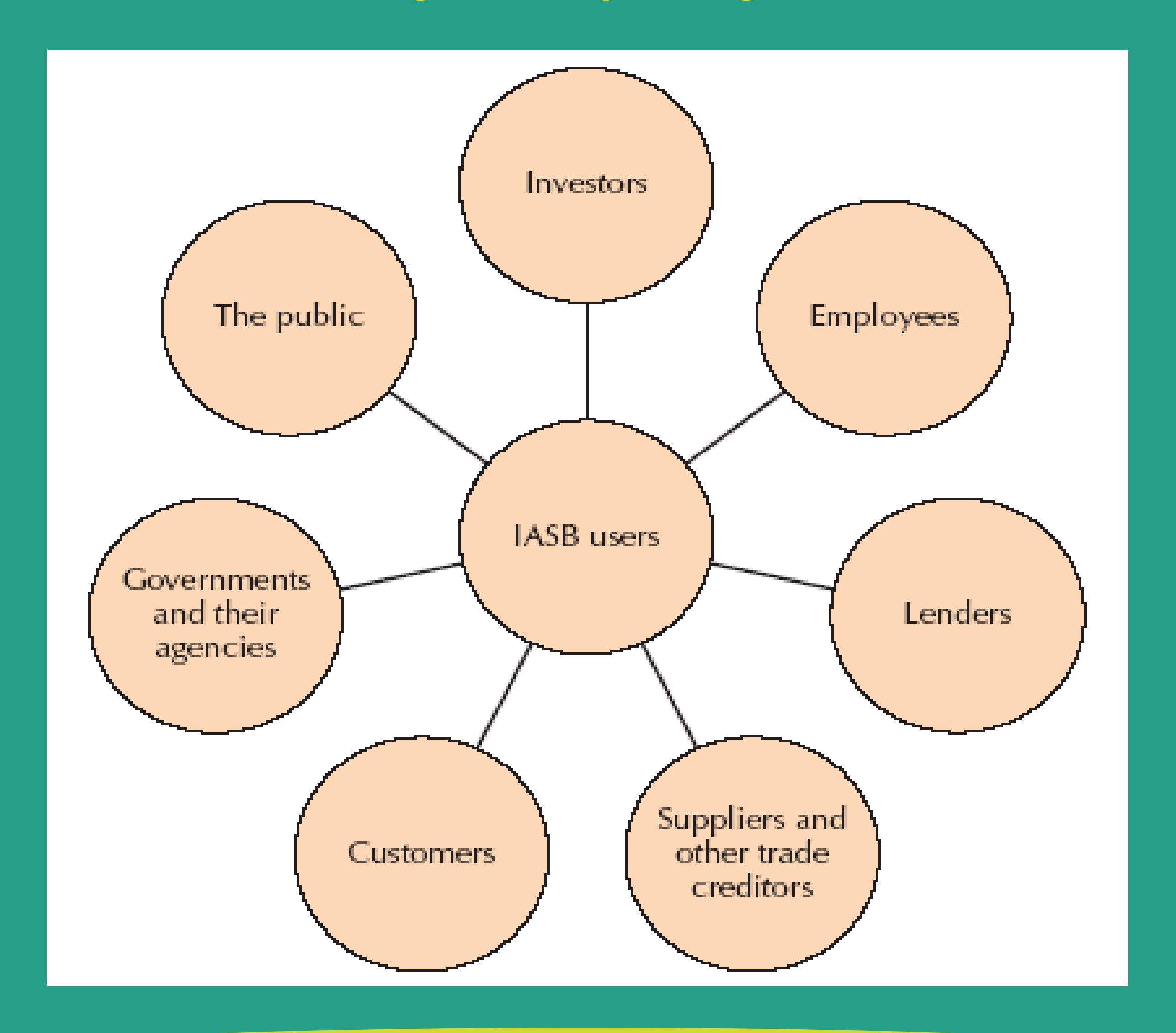
Accounting for International Differences

- Accounting Objectives
- Factors in International Accounting Practices
- Cultural Differences in Accounting
- Classifying Accounting Systems
- International Standards and Global Convergence
- The International Accounting Standards Board

Accounting Objectives

- Identify, record, and interpret economic events
- The Financial Accounting Standards Board (FASB)
- The International Accounting Standards Board (IASB)
- Who uses accounting information?

Who Uses Accounting Information?



Factors Influencing International Accounting Practices

Other external users
1. Creditors
2. Institutional investors
3. Noninstitutional investors
4. Securities exchange

Enterprise users
1. Management
2. Employees
3. Supervisory councils
4. Board of directors

Nature of the enterprise
1. Form of business organization
2. Operating characteristics

Accounting profession
1. Nature and extent of profession
2. Professional associations
3. Auditing

Development of accounting objectives, standards, and practices

Characteristics of the local environment
1. Rate of economic growth
2. Inflation rate
3. Public versus private ownership and control of the economy
4. Cultural attitudes

International influences
1. Colonial history
2. Foreign investors
3. International Accounting Standards Board
4. Regional cooperation
5. Regional capital markets

Academic influences
1. Educational infrastructure
2. Basic and applied research
3. Academic associations

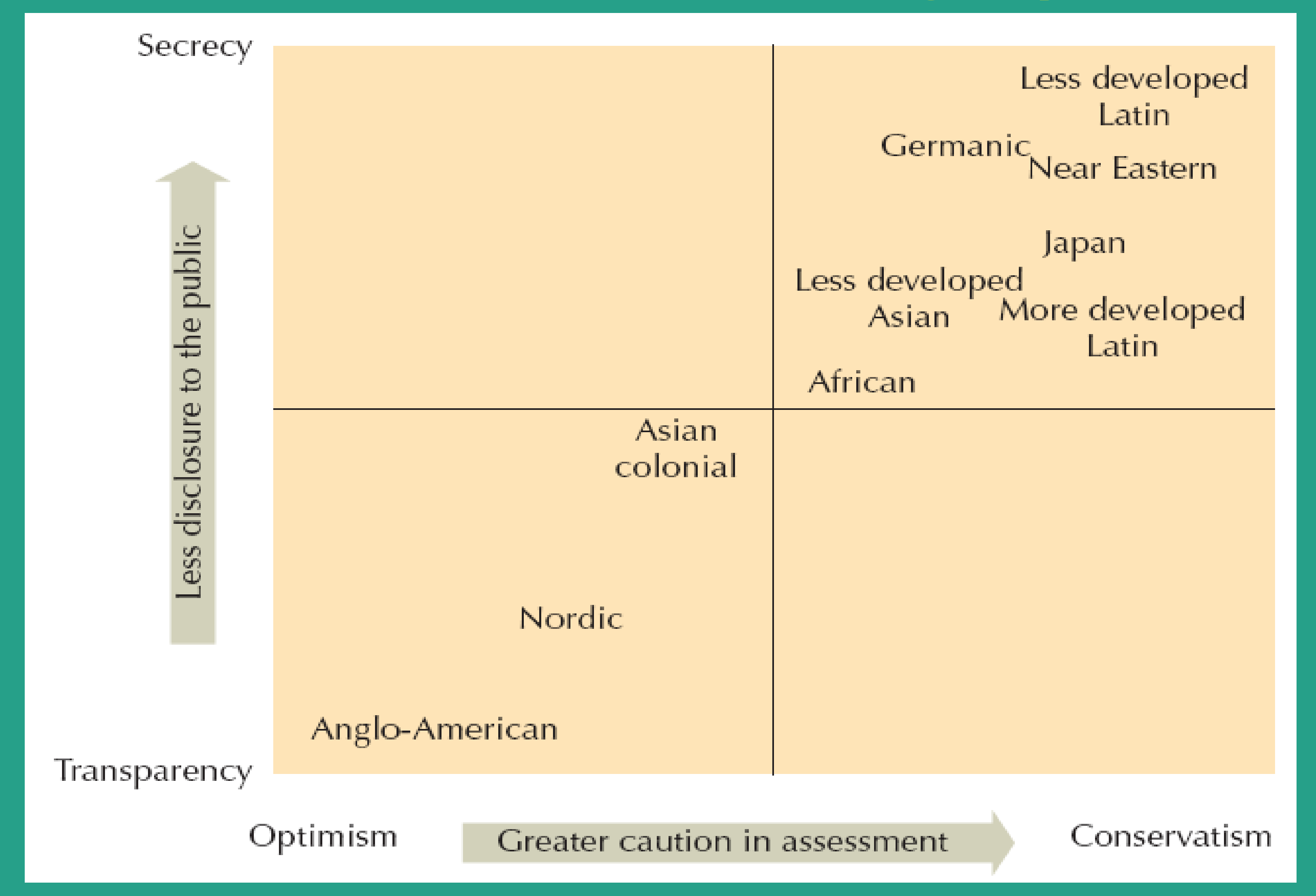
Government
1. Users and tax planners
2. Regulators

Cultural Differences in Accounting

Culture influences measurement and disclosure practices:

- Measurement—how to value assets
- Disclosure—the presentation of information and discussion of results

Disclosure/Assessment Matrix for National Accounting Systems



Classifying Accounting Systems

- From Macro-Uniform to Micro Based Systems
- Strong versus Weak Equity Markets
- Differences in Financial Statements
  - Language
  - Currency
  - Type of statements
  - Financial statement format
  - Extent of footnote disclosures
  - Underlying GAAP on which the financial statements are based

Reporting Differences

Major approaches to dealing with accounting and reporting differences:

- Mutual recognition
- Reconciliation to local GAAP
- Recasting of financial statements in terms of local GAAP

International Standards and Global Convergence

Major forces leading to convergence:

- Investor orientation
- Global integration of capital markets
- MNEs’ need for foreign capital
- Regional political and economic harmonization
- MNEs’ desire to reduce accounting and reporting costs
- Convergence efforts of standards-setting bodies

International Accounting Standards Board

- The relationship between the FASB and IASB
- The European Response to Convergence
- Convergence and Mutual Recognition

Transactions in Foreign Currencies

- Recording Transactions
- Correct Procedures for U.S. Companies

Translating Foreign Currency Financial Statements

- Translation Methods
  - Temporal Method: applies when the parent's reporting currency is the functional currency.
  - Current Rate Method: applies when the local currency is the functional currency.

Managing Accounting Issues

- Performance, Evaluation, and Control
- Transfer Pricing and Performance Evaluation
- The Balanced Scorecard

Corporate Governance

- External Control Mechanism: The Legal System
- Internal Control Mechanisms

Future: Will IFRS Become the Global Accounting Standard?

- IFRS is modeled after capital market orientation of U.K. and U.S.
- More companies are choosing to list on the European stock markets
- Sarbanes-Oxley Act 2002